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The UK housing market and stamp duty reform.

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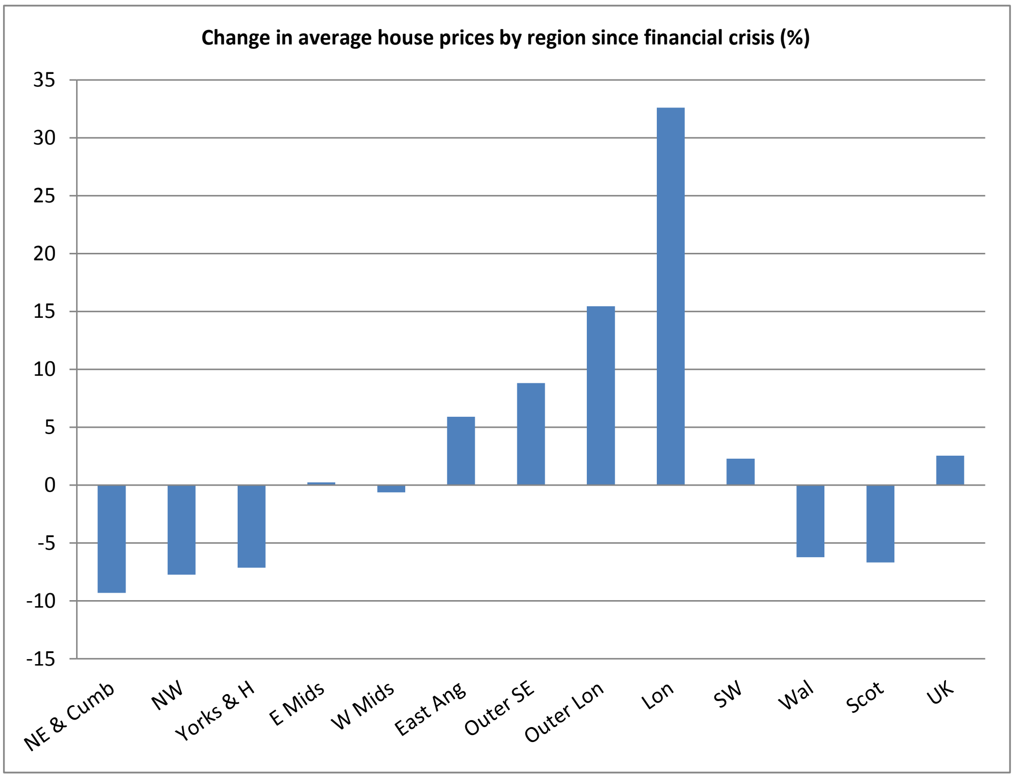
In this Brief, the Sheffield Political Economy Research Institute assesses evidence on trends within the UK housing market since the financial crisis. It concentrates in this regard on regional differences within the apparent housing market recovery, and considers what these differences indicate about the nature of the UK's post-crisis growth model. The Brief also assesses the regional impact of the coalition government's recent changes to stamp duty on housing transactions – announced in December 2014 – and considers what this measure tells us about the government's economic stewardship.

Background

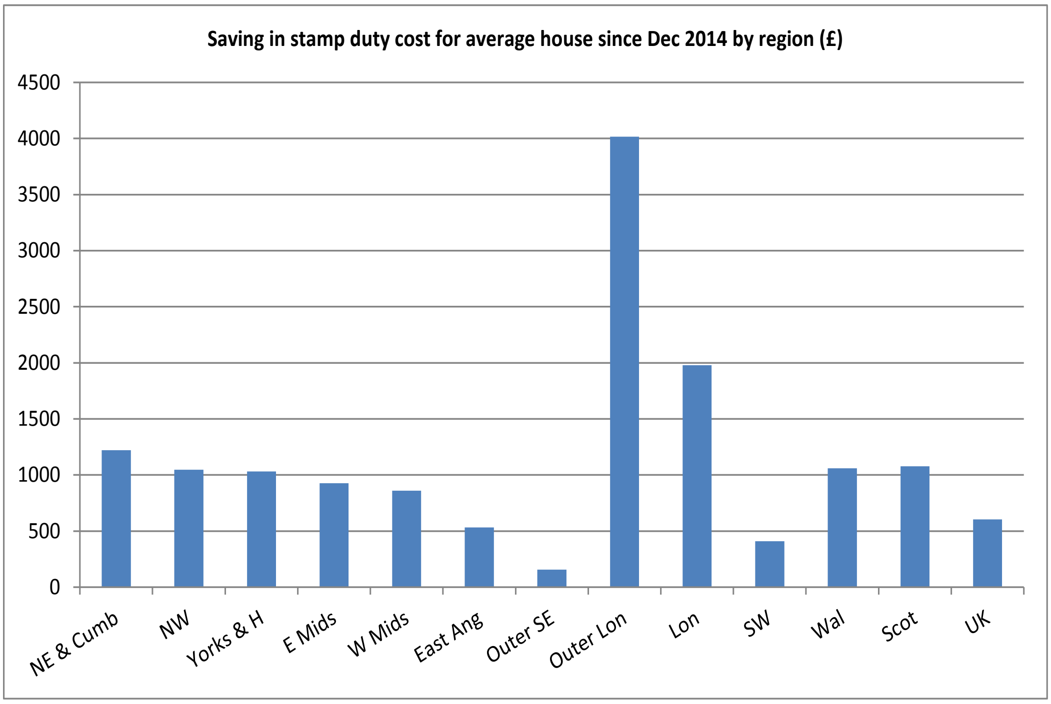
- The housing market was central to the model of economic growth evident in the UK before the financial crisis. Rising property values compensated for stagnating earnings and helped to fuel high levels of consumer spending (Hay, 2013).
- The exemption of housing transaction from capital gains tax enabled this scenario to some extent, yet the levy of stamp duty on house purchases nevertheless meant the housing market was also an important source of tax revenue.
- Yet the pre-crisis housing market boom is also associated with several acute economic problems. It exacerbated regional inequality as high property values in London led to a greater concentration of wealth in the capital.
- It also led to UK banks focusing lending on mortgages at the expense of productive activity and created significant concerns around housing affordability, especially for young people and low-earners.
- There is clearly a need, therefore, to consider whether such problems have abated in the post-crisis environment. A more sustainable recovery in the UK economy may depend on reducing dependence on the housing market.
- However, enabling home-ownership has been a central part of the coalition government's economic agenda, as demonstrated by the Help to Buy scheme. Importantly, the mortgage guarantee element of Help to Buy is available to anybody buying a home valued under £600,000, not simply first-time buyers. Help to Buy was extended last year until 2020.
- A reform of stamp duty was announced by the Chancellor of the Exchequer, George Osborne, in the Autumn Statement in late 2014.
- Under the previous system, people buying a house costing between £125,000 and £250,000 paid 1 per cent of the cost in stamp duty. There was then a significant 'cliff edge', with a 3 per cent rate applied to houses costing between £250,000 and £500,000 (higher rates were applied above this point).
- Under the new system, introduced overnight on 4 December 2014, an allowance of £125,000 is applied to every housing transaction. Stamp duty of 2 per cent is applied beyond the first £125,000, up to £250,000, and 5 per cent is applied from £250,000 to £925,000 (higher rates apply after this point).

Evidence

- The chart below shows that the housing market recovery is strongest in London and, to a lesser extent, the wider South East region. Average house prices are now more than 30 per cent above their pre-crisis peak in inner London, more than 15 per cent above in outer London, and almost 9 per cent above in the rest of the South East.
- In contrast, average house prices in the three regions of Northern England remain 5-10 per cent below their pre-crisis peak. The post-crisis trends have therefore reinforced regional housing market inequalities evident before the financial crisis.



- In terms of lending by UK banks, the amount loaned to individuals secured on dwellings (i.e. mortgages) has risen from 28 per cent of all lending before the financial crisis, to almost half by the end of 2014 (46 per cent) (Bank of England, 2015).
- It was in this context that the coalition government decided to reform stamp duty on property at the Autumn Statement in December 2014. The chart below shows that the new system disproportionately benefits home-buyers in London, particularly the outer London area.
- People buying averagely priced houses in inner London can expect to pay around £2,000 less in stamp duty, and people in outer London can expect to pay around £4,000 less.
- In contrast, people buying averagely priced houses in the Midlands and Northern England can expect to pay around £1,000 less.



- The change is also expected to reduce tax revenues by around £800 million per year (HM Treasury, 2014).
- The unbalanced housing market recovery means that, in most places outside London and the South East, house prices have become slightly more affordable for lower earners (although this does not mean that sufficient housing is available).
- As the table in the annex shows, the ratio of median house prices to median earnings, and the ratio of lower quartile house prices and lower quartile earnings, fell significantly between 2007 and 2013 throughout Northern England and the Midlands (although they remain high in historical terms).
- In London, however, both ratios have increased over this period. Even at the lower end, the housing market is outpacing earnings growth, and residential property is therefore becoming less affordable for lower earners in the capital.

Analysis

- Given that a housing market crash was one of the main triggers of the financial crisis and subsequent economic stagnation, there is a clear need to reduce the UK economy's dependence on housing market growth.
- However, the apparent UK housing market recovery has been based on a re-ignition and intensification of trends evident before the financial crisis.
- Most alarmingly, the recovery has been led almost exclusively by the acceleration of house prices in London and the South East – reinforcing regional inequalities and exacerbating the problem of unaffordable housing for low earners in the capital.

- Housing has actually become more affordable for lower earners elsewhere in the UK – hugely undermining the political case for Help to Buy.
- The banking sector – despite being part-nationalised in 2008 – now appears even more oriented towards mortgage lending than investment in productive activity.
- The coalition government's decision to reform stamp duty on housing transactions in late 2014 will only reinforce these trends. It provides a fiscal boost to the housing market throughout the UK, further dis-incentivising the 'rebalancing' of the UK economy.
- Moreover, it will mainly benefit homebuyers in London. In the long term, this will strengthen regional inequalities as the London housing market continues to boom. But in the short term, as the general election approaches, it also offers a hugely significant tax cut for households in London's commuter belt.
- This manoeuvre not only contradicts efforts to rebalance the economy, but also brings into question the coalition's commitment to austerity.

Conclusion

The evidence assessed here suggests that the UK housing market has returned to 'business as usual'. This can be seen as a sign of economic recovery, yet, equally, it also suggests that many of the problems associated with the onset of the financial crisis and subsequent stagnation remain salient. The coalition government's decision to reform – and, in effect, significantly reduce – stamp duty indicates that it is relatively unconcerned by the economy's dependence on the housing market and the continuing acute regional inequalities which pervade the UK growth model.

References

Bank of England (2015) *Bankstats: December 2015*, available at http://www.bankofengland.co.uk/statistics/Pages/bankstats/default.aspx.

HM Treasury (2014) *Autumn Statement 2014: Policy Costings*, available at https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/384071/AS2014_policy_costings_final.pdf.

Hay, C (2014) *The Failure of Anglo-Liberal Capitalism* (Basingstoke: Palgrave).

Annex

Change in average house prices by region since the financial crisis

	NE & Cumb	NW	Yorks & H	E Mids	W Mids	East Ang	Outer SE	Outer Lon	Lon	SW	Wal	Scot	UK
Q3 2007 (£000s)	135	159	155	157	165	184	215	259	302	204	154	152	184
Q3 2014 (£000s)	122	147	145	157	164	195	234	299	401	209	144	142	189
% change	-9.3	-7.7	-7.1	0.2	-0.6	5.9	8.8	15.4	32.6	2.3	-6.2	-6.7	2.5

Source: Nationwide House Price Index (http://www.nationwide.co.uk/about/house-price-index/headlines)

Cost of stamp duty for average house by region (£)

	NE & Cumb	NW	Yorks & H	E Mids	W Mids	East Ang	Outer SE	Outer Lon	Lon	SW	Wal	Scot	UK
Old system	1220	1453	1468	1573	1641	1947	2344	8946	12032	2041	1449	1423	1881
New system	0	405	435	646	781	1394	2167	4928	10054	1682	382	346	1276
Saving	1220	1047	1032	927	859	533	156	4017	1978	409	1059	1077	605

Source: SPERI calculations based on Nationwide House Price Index (see above for link)

Ratio of median/lower quartile house price to median/lower quartile earnings (selected areas)

		Tyne & Wear	Gtr Manc	Merseyside	S Yorks	W Yorks	Notts	W Mids	Inner London	Outer London
Median price/earnings ratio	2007	5.90	5.66	5.76	5.50	5.95	6.16	5.76	9.17	9.04
	2013	4.96	4.94	4.84	4.63	4.95	5.57	5.06	10.41	9.10
Lower quartile price/earnings ratio	2007	5.86	5.92	5.72	5.83	6.24	6.58	6.51	9.45	9.77
	2013	4.72	4.68	4.57	4.59	4.92	5.51	5.37	10.00	9.79

Source: DCLG (https://www.gov.uk/government/statistical-data-sets/live-tables-on-housing-market-and-house-prices)

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